Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Message Text

PAGE 01 STATE 188097
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TO AMEMBASSY TOKYO PRIORITY
INFO USMISSION GENEVA PRIORITY

UNCLAS STATE 188097

E.O. 11652: N/A

TAGS:ETRD, JA, MTN

SUBJECT:TRADE FACILITATION COMMITTEE CASE--CIGAR
ASSOCIATION

REF: (A) STATE 84173 (B) TOKYO 7055 (C) TOKYO 10852

1. SUMMARY: COMMERCE (USDOC) SENDING FINAL VERSION OF
CIGAR CASE ORIGINALLY FORWARDED FOR TFC CONSIDERATION IN
UNCLASSIFIED

PAGE 02 STATE 188097

REFTEL A, BASED ON INFORMATION AND EMBASSY VIEWS CONTAINED
IN REFTELS B AND C. THIS CASE IS TO BE SUBMITTED AND
DISCUSSED SEPARATELY FROM TFC CASE NO. 5 ON CIGARETTES.
END SUMMARY.

2. MICHAEL J. KOWALSKY, VICE PRESIDENT OF THE CIGAR
ASSOCIATION OF AMERICA, INC., WROTE USDOC MAY 10 TO
COMMENT ON GOJ RESPONSE TO TFC CASE NO. 5 ON CIGARETTES.
(LETTER WITH ENCLOSURE BEING SENT TO EMBASSY; TABLES I-IV
REFERRED TO BELOW ALSO BEING SENT.) IN CONVERSATIONS WITH

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

USDOC OFFICIAL WEEK OF MAY 8, KOWALSKY AND CARL J. CARLSON, PRESIDENT OF THE CIGAR ASSOCIATION, RECOMMENDED THAT A RESOLUTION OF GOJ RESTRICTIONS ON CIGAR IMPORTS SHOULD BE REQUESTED IN THE TFC AS WELL AS IN THE MTN AND THAT SUCH A TFC REQUEST SHOULD BE SEPARATED FROM THAT ON

CIGARETTES. (THE MAJOR REASON FOR HANDLING CIGARS SEPARATELY FROM CIGARETTES IS THAT THE MARKET FOR PROCESSING TOBACCO TO MANUFACTURE CIGARS IN JAPAN IS RELATIVELY SMALL; THIS IN TURN MEANS THAT A FAVORABLE RESOLUTION OF THE CIGAR CASE SHOULD NOT SIGNIFICANTLY DISRUPT THE MAJOR PART OF THE JAPANESE LEAF PROCESSING INDUSTRY, I.E., CIGARETTES, NOR UPSET AMERICAN EXPORTERS OF LEAF TOBACCO). INFORMATION PROVIDED BY EMBASSY ON CIGAR PRICES EFFECTIVE JULY 1, 1978 IN REFTEL C MOST HELPFUL TO COMMERCE AND CIGAR ASSOCIATION IN PREPARING FINAL CASE.

3. TEXT OF TFC CASE ON BEHALF OF CIGAR ASSOCIATION TO BE PRESENTED TO JAPANESE OFFICIALS IN TFC ALONG THE FOLLOWING LINES: BEGIN TEXT

A. SUMMARY OF CASE: VARIOUS PRACTICES OF THE JAPAN

TOBACCO AND SALT PUBLIC CORPORATION (JTS), UNDER THE MINISTRY OF FINANCE (MOF), HAVE A DISCRIMINATORY AND RESTRICTIVE IMPACT ON JAPANESE IMPORTS OF FOREIGN CIGARS (BTN 24.02-110), MOST OF WHICH ARE SUPPLIED BY AMERICAN EXPORTERS. THESE PRACTICES INCLUDE THE PRICING POLICIES OF JTS, THE SMALL NUMBER OF DISTRIBUTORS AND OTHER OUTLETS, AND LIMITATIONS ON THE SIZES AND SHAPES OF IMPORTED CIGARS. THE PRICING POLICIES OF JTS, WHICH INVOLVE UNREASONABLY HIGH WHOLESALE MARKUPS ON IMPORTED CIGARS RESULTING IN RETAIL PRICES THAT DO NOT REFLECT NORMAL COMMERCIAL CONSIDERATIONS, CONSTITUTE BY FAR THE PRINCIPAL NON-TARIFF BARRIER TO THE EXPORT OF U.S. CIGARS.

B. FACTS OF THE CASE:

(1) DISCRIMINATORY JTS PRICING POLICIES: THE PRICING POLICIES OF JTS CONTAIN ELEMENTS WHICH DISCRIMINATE AGAINST THE IMPORTATION AND SALE OF FOREIGN CIGARS AT THE WHOLESALE AND RETAIL LEVELS. FIRST, ACCORDING TO JTS, 70 PERCENT OF THE RETAIL PRICE OF IMPORTED CIGARS CONSTITUTES REVENUE FOR MOF, AS CONTRASTED WITH 60-65 PERCENT FOR DOMESTIC BRANDS. THIS 70 PERCENT REVENUE LEVEL FOR IMPORTS IS OBTAINED BY EXTRAORDINARILY HIGH WHOLESALE MARKUPS. SECOND, JTS ALLOWS RETAIL PROFIT MARGINS OF SEVEN PERCENT ON IMPORTED CIGARS AS AGAINST TEN PERCENT ON DOMESTIC BRANDS. A MORE DETAILED ANALYSIS OF THE PRICING POLICIES OF JTS AT WHOLESALE

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

AND RETAIL LEVELS WITH RESPECT TO IMPORTED CIGARS, AS
COMPARED TO BOTH DOMESTIC BRANDS AND SALE OF THE IMPORTED
BRANDS IN THE UNITED STATES, POINTS TO THEIR RESTRICTIVE
EFFECT ON U.S. EXPORTS OF CIGARS TO JAPAN (SEE PARAS 2-4

IMMEDIATELY FOLLOWING).

(2) HIGH JTS MARKUPS ON IMPORTS AT WHOLESALE LEVEL:
TABLE I LISTS THE PRICES AT VARIOUS LEVELS OF U.S. CIGARS
UNCLASSIFIED

IMPORTED INTO JAPAN AND SIMILAR PRICES FOR SOME JAPANESE
DOMESTIC BRANDS BASED ON JTS RETAIL PRICES EFFECTIVE
JULY 1, 1978, AND JTS ESTIMATES OF MOF REVENUE AND
RETAILER PROFIT MARGINS. INFORMATION ON THE COSTS TO
JTS AND ON THE WHOLESALE MARKUP OF DOMESTIC BRANDS
IS NOT AVAILABLE. HOWEVER, THE JTS MARKUPS ON IMPORTED
U.S. BRANDS RANGE FROM 486 PERCENT TO 664 PERCENT.
IN COMPARING THE TREATMENT OF IMPORTS WITH THAT OF
DOMESTIC BRANDS, WE FIND THAT JTS REVENUE IS 51.8 YEN
PER PIECE FOR THE U.S.-SUPPLIED "MURIEL CORONELLA' BUT
ONLY ABOUT 46.3 YEN FOR THE JAPANESE "PALOMA", EVEN
THOUGH BOTH CIGARS HAVE AN IDENTICAL RETAIL PRICE.
TABLE II PROVIDES DATA ON WHOLESALE PRICING AND MARKUPS
FOR THOSE U.S. BRANDS SOLD IN JAPAN. AS CAN BE SEEN
FROM THE DATA, WHOLESALE MARKUPS IN THE UNITED STATES
ARE ABOUT 16PERCENT FROM WHOLESALE COST AND 29 PERCENT
FROM NET FACTORY COST (EXCLUDES EXCISE TAX). TABLE III
USES THE DATA IN TABLES I AND II TO COMPARE PRICING OF THE
U.S. BRANDS IN THE JAPANESE AND U.S. MARKETS. U.S.
WHOLESALE LIST FOR THE SIX BRANDS RANGE FROM ABOUT
FIVE CENTS TO EIGHT CENTS PER CIGAR, WHEREAS JTS
WHOLESALES THESE SAME CIGARS AT PRICES RANGING FROM
ABOUT 27 CENTS TO 50 CENTS DESPITE THE FACT THAT THE
COST OF THESE CIGARS TO BOTH U.S. WHOLESALERS AND JTS,
IS ROUGHLY EQUAL. EVEN IF WE CALCULATE U.S. WHOLESALE
MARKUPS FROM NET FACTORY COST, THE JTS WHOLESALE MARKUPS
ARE SOME 16-22 TIMES HIGHER. TABLE IV SHOWS THE ACTUAL
WHOLESALE MARKUP BY JTS AS CONTRASTED WITH THE EFFECT
OF THE 200 PERCENT DUTY, WHICH IS NOT APPLIED TO
JTS PURCHASES SINCE JTS IS AN ARM OF MOF. BASED ON THE
JTS ESTIMATES WHICH WE PREVIOUSLY RECEIVED, THE PRICING
POLICIES OF JTS AT WHOLESALE APPEAR TO BE THE EQUIVALENT
OF A DUTY OF SOME 365 PERCENT, WELL ABOVE THE STATUTORY
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RATE OF 200 PERCENT.

(3) HIGH JTS MARKUPS ON IMPORTS AT RETAIL LEVEL: TABLE
I SHOWS THE RESULT OF JTS ALLOWING A RETAIL PROFIT MARGIN

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

OF ONLY SEVEN PERCENT ON IMPORTED CIGARS AS CONTRASTED WITH TEN PERCENT ON DOMESTIC BRANDS. FOR EACH THOUSAND JAPANESE-PRODUCED "PALOMAS" SOLD AT 74 YEN PER PIECE, A RETAILER HAS A MARGIN OF 7400 YEN, WHEREAS FOR ONE THOUSAND AMERICAN "MURIEL CORONELLAS" (WHICH HAVE AN IDENTICAL RETAIL PRICE OF 74 YEN PER PIECE), A RETAILER HAS A MARGIN OF ONLY 5200 YEN. ANOTHER EXAMPLE IS THE

COMPARISON IN MARGIN PER THOUSAND CIGARS FOR THE JAPANESE-PRODUCED "BARCA" AND THE AMERICAN "KING EDWARD DELUXE". THE MARGIN OF 6400 YEN FOR THE JAPANESE BRAND EXCEEDS THAT FOR THE AMERICAN BRAND (5600 YEN), EVEN THOUGH THE RETAIL PRICE PER PIECE OF 80 YEN FOR THE AMERICAN BRAND IS MUCH HIGHER THAN THAT (60 YEN) FOR THE "BARCA". THESE COMPARISONS INDICATE THAT RETAILERS HAVE A SIGNIFICANTLY HIGHER MARGIN ON JAPANESE DOMESTIC BRANDS OF COMPARABLE OR LOWER RETAIL PRICE THAN ON IMPORTED CIGARS MADE IN THE UNITED STATES. TABLE III ILLUSTRATES THAT THE MARKUP AT THE RETAIL LEVEL IS NOT NEARLY AS SEVERE AS AT THE WHOLESALE LEVEL (COLUMNS 3 AND 5). NEVERTHELESS, THERE IS A FAIRLY CONSISTENT PATTERN OF THE U.S. BRANDS BEING MARKED UP FROM WHOLE-SALE LIST TO RETAIL BY ABOUT ONE DOLLAR TO ONE DOLLAR AND FIFTY CENTS PER THOUSAND IN THE U.S. MARKET, WHEREAS THE RETAIL MARKUP IN JAPAN (FROM A MUCH HIGHER JTS WHOLESALE LEVEL) AVERAGES ABOUT TWO DOLLARS TO THREE DOLLARS PER THOUSAND.

(4) JTS MARKUPS ON IMPORTS AS COMPARED WITH U.S. MARKUPS:

TABLE III ALSO ILLUSTRATES THAT JTS MARKUPS ON IMPORTS FROM THE U.S. AT EACH LEVEL, PARTICULARLY WHOLESALE,
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AND OVERALL ARE EXTREMELY HIGH AS COMPARED WITH MARKUPS ON THE SAME U.S. CIGARS IN THE U.S. MARKET WHERE THERE IS NO STATE MONOPOLY TO SET PRICES. COLUMNS (1) AND (2) INDICATE THAT JTS RECEIVES THESE CIGARS AT ROUGHLY THE SAME PRICE AS ANY U.S. WHOLESALER. COLUMNS (3) AND (4) SHOW THE COMPARABLE LIST PRICES OF U.S. WHOLESALERS AND JTS AND THE MARKUPS INVOLVED. MOST OF THESE CIGARS LIST FOR WHOLESALE IN THE U.S. AT ABOUT SIX CENTS AT A 29 PERCENT MARKUP FROM NET FACTORY COST (L16 PERCENT FROM WHOLESALE COST), AND LIST WHOLESALE IN JAPAN AT ABOUT 30 CENTS AT MARKUPS OVER 500 PERCENT FROM WHOLE-SALE COST. COLUMNS (5) AND (6) PRESENT THE RETAIL PRICES AND TOTAL MARKUP FROM WHOLESALE COST TO RETAIL. AGAIN, MOST OF THESE CIGARS RETAIL IN THE U.S. FOR ABOUT SEVEN AND ONE HALF CENTS AT ROUGHLY A 40 PERCENT MARKUP AND RETAIL IN JAPAN FOR ABOUT 30 CENTS AT MARKUPS OF OVER 530 PERCENT. THE HIGHER-PRICED "HAVATAMPA JEWEL" PROVIDES AN EXCEPTION TO THESE AVERAGES IN THAT

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

IT LISTS AT WHOLESALE IN JAPAN FOR ABOUT 50 CENTS AT A 664 PERCENT WHOLESALE MARKUP AND RETAILS FOR ABOUT 54 CENTS AT A 792 PERCENT MARKUP THOUGH RETAIL. YET IN THE UNITED STATES THIS SAME CIGAR LISTS AT WHOLESALE FOR ABOUT EIGHT CENTS AND AT RETAIL FOR ABOUT TEN CENTS WITH A TOTAL MARKUP THROUGH RETAIL OF 43 PERCENT.

(5) JTS PRICING NOT IN STEP WITH THE APPRECIATION OF THE YEN: IN 1972, THE YEN/DOLLAR EXCHANGE RATE WAS YEN 303.1 $1.00 AND IN APRIL 1978 IT WAS YEN 221.7 $1.00 -- A YEN APPRECIATION OF ABOUT 36 PERCENT. IN 1972, THE ROBERT BURNS CIGARILLO RETAILED IN THE US FOR SIX CENTS AND IN JAPAN FOR 20 CENTS. TODAY, THIS CIGAR STILL RETAILS IN THE U.S. FOR SIX CENTS BUT RETAILS IN JAPAN FOR 29 CENTS. IN OTHER WORDS, DESPITE THE APPRECIATION
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OF THE YEN BY OVER ONE-THIRD BETWEEN 1972 AND 1978, JTS HAS RAISED THE PRICE OF AN IMPORTED CIGAR BY 50 PERCENT IN DOLLAR TERMS.

(6) JTS ALLOWS ONLY A VERY SMALL NUMBER OF OUTLETS FOR IMPORTED CIGARS: TOBACCO PRODUCTS IN JAPAN ARE SOLD THROUGH 249,000 JTS AUTHORIZED RETAIL SHOPS, SOME 200,000 VENDING MACHINES, AND AN UNKNOWN NUMBER OF RESTAURANT, HOTEL, TRAIN STATIONS AND OTHER KIOSKS. JTS AUTHORIZES A LIMITED NUMBER OF HIGH VOLUME RETAIL SHOPS (14,100 AS OF SEPTEMBER 1977) TO SELL IMPORTED TOBACCO PRODUCTS. OF THESE, JTS SOURCES ESTIMATE LESS THAN HALF HANDLE CIGARS AND THAT A MUCH SMALLER NUMBER HANDLES IMPORTED BRANDS. INDUSTRY SOURCES IN TOKYO ESTIMATE THAT ONLY ABOUT 1500-2000 HIGH-VOLUME RETAIL SHOPS HANDLE IMPORTED CIGARS, AND ONLY 400-500 MORE THAN ONE IMPORTED BRAND, I.E., MUCH LESS THAN ONE PERCENT OF RETAIL SHOPS HANDLE IMPORTED CIGARS. WHILE JTS LICENSING OF SHOPS TO HANDLE IMPORTED CIGARETTES IS APPARENTLY BASED ON THE RULE THAT AT LEAST 30 CARTONS PER MONTH MUST BE SOLD, WE ARE NOT AWARE OF THE CRITERION USED TO AUTHORIZE HANDLING OF FOREIGN CIGARS.

(7) JTS LIMITS THE SIZES AND SHAPES OF IMPORTED U.S. BRANDS TO SIX: THE SIX AMERICAN CIGARS (CIGARILLOS) LISTED IN TABLES I-IV ARE THE ONLY ONES AUTHORIZED FOR SALE IN JAPAN. IN COMPARISON, THERE ARE OVER 500 BRANDS OF CIGARS SOLD IN THE U.S. MARKET. NO FULL-SIZED AMERICAN CIGARS CAN BE SOLD IN JAPAN. JTS RESTRICTS SALES OF LARGE CIGARS MOSTLY TO THE JAPANESE DOMESTIC BRANDS WHICH RETAIL BETWEEN ABOUT 45 CENTS AND ABOUT ONE DOLLAR AND SIXTY-TWO CENTS PER PIECE. COMPARABLE U.S. LARGE CIGARS RETAIL IN THE U.S. FOR BETWEEN ABOUT TEN CENTS AND ABOUT 30 CENTS PER PIECE.

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

(8) JAPANESE CIGAR PRODUCTION, SALES, AND IMPORTS AND U.S. CIGAR EXPORTS TO JAPAN: ACCORDING TO JTS FIGURES, JAPANESE CIGAR PRODUCTION, DOMESTIC SALES AND IMPORTS (IN THOUSANDS OF UNITS) HAVE BEEN AS FOLLOWS:

TABLE A

JFY	PRODUCTION	SALES	IMPORTS
1971	8,950	9,119	10,003
1972	21,652	18,323	10,893
1973	31,454	27,323	11,985
1974	28,970	28,962	12,592
1975	19,914	20,012	8,341
1976	34,054	29,477	6,069
1977	(NOT AVAILABLE)		5,152
TOTAL'71-1977	N.A.	N.A.	65,035

ACCORDING TO JAPANESE TRADE DATA BY CALENDAR YEAR FOR "CIGARS AND CHEROOTS; CIGARILLOS", JAPAN'S IMPORTS FROM THE WORLD AND THE U.S. (IN THOUSANDS OF UNITS) HAVE BEEN AS FOLLOWS:

TABLE B

CY	WORLD TOTAL	U.S.	VALUE (IN DOLLARS)
1971	7,426	6,330	227.4
1972	11,548	9,515	354.4
1973	15,075	11,490	436.9
1974	11,416	9,178	372.1
1975	9,056	6,704	303.5

1976	3,427	2,709	129.6
1977	3,577	2,668	143.3
TOTAL	61,525	48,594	1,967.2

(IN THOUSANDS OF DOLLARS CONVERTED AT YEN/DOLLAR EXCHANGE RATES OF YEN 350.7, 303.1, 271.2, 291.5, 296.8, 296.6, AND 268.5 (EQUAL ONE DOLLAR) RESPECTIVELY FOR 1971-1977.

ACCORDING TO U.S. TRADE DATA, U.S. EXPORTS OF CIGARS TO JAPAN AND THE REST OF THE WORLD FOR THE SAME PERIOD HAS BEEN (IN THOUSANDS OF UNITS):

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

TABLE C REST OF

	QTY	VALUE (DOLLARS)	WORLD	TOTAL
,971	8,837	302.3	39,797	48,634
1972	17,452	646.6	57,946	75,398
1973	44,510	1060.0	63,512	108,022
1974	19,697	766.4	66,767	86,464
1975	15,820	697.7	116,019	131,839
1976	16,877	449.8	107,557	124,434
1977	6,560	248.2	110,158	116,718
TOTAL	129,753	4171.0		

IF THE JAPANESE DATA IN TABLES A AND B ARE USED, THEY INDICATE THAT IMPORTS HAVE DECLINED TO ABOUT 17 PERCENT OF THE MARKET IN 1976 FROM OVER 50 PERCENT OF THE MARKET IN 1971. IN FACT, IMPORTS HAVE ALMOST BEEN CUT IN HALF WHILE DOMESTIC PRODUCTION AND SALES HAVE GROWN OVER THREEFOLD. IN OTHER WORDS, THE JAPANESE GOVERNMENT HAS ENCOURAGED DOMESTIC PRODUCTION TO TAKE NOT ONLY ALL OF THE GROWING CIGAR MARKET IN JAPAN BUT EVEN TO CROWD OUT IMPORTS, DESPITE THE FACT THAT IMPORTS, IN THE ABSENCE OF THE HIGH PROTECTIONIST EFFECT OF JTS PRICING POLICIES (EQUIVALENT TO ROUGHLY A 365 PERCENT TARIFF AS SEEN ABOVE IN TAB IV), WOULD HAVE BEEN ABLE TO COMPETE FOR A CONSTANT AND PROBABLY INCREASING SHARE OF THE MARKET.
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IF WE USE THE U.S. DATA FOR EXPORTS TO JAPAN AND THE REST OF THE WORLD (WHICH DIFFER SIGNIFICANTLY FROM JAPANESE DATA ON IMPORTS FROM THE U.S. FOR SOME UNKNOWN REASON), WE STILL FIND THAT U.S. EXPORTS TO JAPAN HAVE BEEN FALLING DRASTICALLY FROM THEIR 1973 HIGH. FURTHER-MORE, U.S. EXPORTS TO JAPAN HAVE FALLEN DURING 1973-77 EVEN THOUGH U.S. EXPORTS TO THE WORLD HAVE RISEN SLIGHTLY. THIS AGAIN INDICATES THAT U.S. EXPORTS OF CIGARS TO JAPAN HAVE SUFFERED FROM THE ADVANTAGE GIVEN JAPANESE DOMESTIC PRODUCTION BY JTS POLICIES.

(9) U.S. EXPORT POTENTIAL TO JAPAN FOR CIGARS:

WITHIN FIVE YEARS, THE TOTAL JAPANESE MARKET FOR CIGARS COULD REACH 300 MILLION UNITS FROM THE PRESENT LEVEL OF ABOUT 31 MILLION UNITS (JTS ESTIMATE), GIVEN REASONABLE PRICES AND ACCESS TO CONSUMERS. U.S. EXPORTS MIGHT RISE TO 150-200 MILLION UNITS UNDER SUCH CONDITIONS, REPRESENT-ING 7.5-10.0 MILLION DOLLARS IN INCREASED EXPORT REVENUE. IN THE LONGER TERM, THE TOTAL MARKET MIGHT REACH ONE BILLION UNITS WITH ADDITIONAL U.S. EXPORT GAINS OF PERHAPS 25 MILLION DOLLARS.

C. DISCUSSION

(1) JTS PRICING POLICIES UNREASONABLE AND

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

DISCRIMINATORY AGAINST IMPORTS: THE JAPANESE GOVERNMENT PRACTICES LISTED ABOVE, PARTICULARLY THE PRICING POLICIES OF JTS, CONSTITUTE UNREASONABLE AND DISCRIMINATORY RESTRICTIONS UPON U.S. EXPORTERS OF CIGARS TO JAPAN. THE EXTRAORDINARILY HIGH WHOLESALE MARKUPS OF JTS HAVE LITTLE RELATION TO NORMAL COMMERCIAL CONSIDERATIONS AND ARE OBVIOUSLY DESIGNED TO PROTECT JAPANESE DOMESTIC UNCLASSIFIED

PRODUCTION AND REDUCE CONSUMER DEMAND FOR IMPORTS. THESE MARKUPS RESULT IN A HIGHER LEVEL OF MOF REVENUE ON IMPORTS THAN ON DOMESTIC BRANDS. ALTHOUGH JTS HAS INDICATED THAT THIS HIGH REVENUE AND WHOLESALE MARKUP (SOME 16-22 TIMES HIGHER THAN IN THE U.S. WITH COMPARABLE COSTS) SHOULD NOT BE CONSIDERED AS JTS PROFITS BUT AS A SUBSTITUTE FOR JAPANESE TARIFFS (THE STATUTORY 200 PERCENT DUTY NOT BEING APPLIED) AND TAXES, THE JAPANESE GOVERNMENT HAS MADE NO OFFER IN THE MULTILATERAL TRADE NEGOTIATIONS TO REDUCE THE DUTY ON CIGARS AND THEREBY, IMPLICITLY, LOWER THE EFFECTIVE RATE OF PROTECTION. INDEED, THE ABOVE CALCULATIONS INDICATE THAT THIS EFFECTIVE LEVEL OF PROTECTION, GIVEN CURRENT JTS PRICING POLICIES, APPROACHES 365 PERCENT.

(2) LOWER RETAIL PROFIT MARGINS ON IMPORTS DISCOURAGE SALES OF IMPORTED CIGARS: THE ALLOWABLE JTS PROFIT MARGIN AT RETAIL LEVEL OF SEVEN PERCENT ON IMPORTS AS COMPARED TO TEN PERCENT ON DOMESTIC BRANDS FURTHER DISCRIMINATE AGAINST IMPORTS BY LESSENING THE INCENTIVE OF RETAILERS TOWARD SALES OF IMPORTS VERSUS DOMESTIC BRANDS.

(3) JTS PRICING UNREASONABLY HIGH AS COMPARED TO U.S. PRICES: THE COMPARISON OF JTS PRICING POLICIES AT WHOLESALE LEVEL, RETAIL LEVEL AND OVERALL WITH PRICES IN THE NON-CONTROLLED U.S. MARKET INDICATES THE EXTENT OF PROTECTION IN THE JAPANESE MARKET AGAINST IMPORTED CIGARS. A U.S. CIGAR WHICH RETAILS FOR AN AVERAGE OF ABOUT 75 DOLLARS PER THOUSAND IN THE UNITED STATES AT A TOTAL MARKUP OF ABOUT 40 PERCENT RETAILS IN JAPAN FOR ABOUT 300 DOLLARS PER THOUSAND AT A TOTAL MARKUP OF OVER 530 PERCENT. DESPITE THE FACT THAT THE WHOLESALE COST TO JTS IS ABOUT THE SAME AS TO U.S. WHOLESALERS. THE HIGH WHOLESALE MARKUPS IN JAPAN RESULT IN RETAIL PRICES FOUR-FIVE TIMES AS HIGH AS THOSE IN THE UNITED UNCLASSIFIED

PRICES FOUR-FIVE TIMES AS HIGH AS THOSE IN THE UNITED STATES FOR THE SAME CIGAR. THESE FACTS POINT TO THE CONCLUSION THAT JTS PRICING POLICIES ON IMPORTED CIGARS

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

CONSTITUTE AN UNREASONABLE LEVEL OF PROTECTION IN
THEMSELVES AND IN COMPARISON TO THE UNITED STATES.
THE RISING PRICE OF JAPANESE IMPORTS OF U.S. CIGARS OVER
THE YEARS DESPITE SUBSTANTIAL APPRECIATION OF THE YEN
AND STABLE U.S. PRICES FURTHER INDICATE THAT THE
CONTROLLED PRICES OF IMPORTED CIGARS ARE SET AT LEVELS
WHICH HAVE ASSURED THAT JAPANESE DOMESTIC PRODUCTION
RATHER THAN IMPORTS WOULD CAPTURE A GROWING SHARE OF
A GROWING CIGAR MARKET, EVEN THOUGH DOMESTIC PRODUCTION
WOULD NOT HAVE BEEN COMPETITIVE IN THE ABSENCE OF HIGH
RATES OF PROTECTION.

(4) JTS RESTRICTIONS ON THE NUMBER OF OUTLETS SUPPORT
RESTRICTIVE PRICING: JTS RESTRICTIONS ON THE NUMBER OF
OUTLETS THAT SELL IMPORTED CIGARS TO LESS THAN ONE PERCENT
OF THE TOTAL NUMBER OF OUTLETS ARE RELATED TO THE OVERALL
EFFORT TO RESTRICT ACCESS OF THE CONSUMER TO FOREIGN
CIGARS AT REASONABLE PRICES. THE NUMBER OF CIGARS SOLD
PER MONTH IN ANY OUTLET IS OBVIOUSLY A FUNCTION OF THE
PRICE OF THOSE CIGARS. SINCE JAPANESE CONSUMERS WOULD
PRESUMABLY PURCHASE A MUCH GREATER NUMBER OF IMPORTED
CIGARS AT A SIGNIFICANTLY LOWER PRICE, THE NUMBER OF
RETAIL SHOPS REQUIRED TO MARKET IMPORTED CIGARS IN JAPAN
WOULD BE MUCH GREATER IF THE PRICING OF IMPORTS WAS
NON-DISCRIMINATORY AND MORE IN LINE WITH NORMAL COMMERCIAL
CONSIDERATIONS.

(5) JTS LIMITATIONS ON NUMBER OF BRANDS ALSO
RESTRICTIVE: THE JTS LIMITATION OF THE NUMBER OF U.S.
BRANDS THAT CAN BE IMPORTED TO SIX SMALL-SIZE CIGARS
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IS A FURTHER RESTRICTION ON IMPORTS OF U.S. CIGARS.
THE GROUNDS FOR THIS LIMITATION ARE NOT CLEAR, BUT WE
DO KNOW THAT EVEN AT THE PRESENT ABNORMALLY HIGH JTS
PRICES, JAPANESE CONSUMERS ARE NOT GIVEN A CHOICE OF
DIFFERENT U.S. BRANDS. AGAIN, GIVEN MORE REASONABLE
PRICES, JAPANESE CONSUMERS WOULD UNDOUBTEDLY DEMAND AN
INCREASING NUMBER OF DIFFERENT BRANDS.

(6) JTS RESTRICTIVE MEASURES HAVE PROTECTED A GROWING
MARKET: THE RESTRICTIVE POLICIES OF JTS, PARTICULARLY
ON WHOLESALE PRICING OF FOREIGN CIGARS, HAVE NOT ONLY
PROTECTED THE JAPANESE CIGAR MARKET FOR JTS' OWN
DOMESTIC PRODUCTION BUT HAVE ALLOWED THAT DOMESTIC
PRODUCTION TO CAPTURE ALL OF THE GROWTH IN THE JAPANESE
CIGAR MARKET SINCE 1971 AD TO INCREASE ITS MARKET SHARE
VIS-A-VIS IMPORTS. THE MAINTENACE OF AN EFFECTIVE RATE
OF PROTECTION OF 365 PERCENT UNDER CONDITIONS OF A
DOUBLING OF THE TOTAL JAPANESE CIGAR MARKET SINCE 1971
HAD NO JUSTIFICATION.

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

Sheryl P. Walter Declassified/Released US Department of State EO Systematic Review 20 Mar 2014

D. RELIEF SOUGHT

(1) THE USG REQUESTS ON BEHALF OF THE CIGAR ASSOCIATION OF AMERICA, INC., AND THE U.S. CIGAR INDUSTRY A FUNDAMENTAL RESTRUCTURING OF JTS PRICING POLICIES, RESTRICTIONS ON OUTLETS AUTHORIZED TO SELL IMPORTED CIGARS, AND LIMITATIONS ON THE NUMBER OF AUTHORIZED BRANDS. SUCH A RESTRUCTURING SHOULD INCLUDE THE FOLLOWING: (A) ELIMINATION OF DISCRIMINATORY PRICING POLICIES, INCLUDING ELIMINATION OF THE DISPARITIES IN REVENUE AND RETAIL PROFIT MARGINS ON IMPORTS VIS-A-VIS DOMESTIC SALES; (B) A SUBSTANTIAL REDUCTION IN THE UNREASONABLY HIGH WHOLESALE MARKUPS APPLIED BY JTS TO IMPORTS SO AS TO BRING THEM MORE INTO LINE WITH U.S. AND NORMAL COMMERCIAL PRICING PRACTICES; (C) JTS EXPANSION IN THE NUMBER OF OUTLETS AUTHORIZED TO SELL IMPORTS
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IN LINE WITH THE INCREASING DEMAND FOR IMPORTS WHICH WOULD RESULT FROM A SIGNIFICANT ALTERATION OF JTS PRICING POLICIES; AND (D) JTS AUTHORIZATION OF INCREASING NUMBERS OF IMPORTED U.S. BRANDS INCLUDING FULL-SIZE CIGARS TO ALLOW FAIR COMPETITION WITH DOMESTIC BRANDS.
END TEXT.

4. WASHINGTON BELIEVES PRESENTATION OF THE CIGAR CASE IN THE TFC APART FROM THE CIGARETTE CASE MAY HELP BOTH SIDES TO FOCUS ON THE NATURE OF THE JTS RESTRICTIONS ON IMPORTS SINCE MANY OF THE ARGUMENTS PREVIOUSLY PRESENTED CONCERNING CIGARETTES HAVE BEEN CLEARLY REBUTTED WITH RESPECT TO CIGARS BY THE ABOVE CASE, OR BY POINTS COVERED IN CIGAR ASSOCIATION COMMENTS BEING FORWARDED. IF JTS CONTINUES TO EMPLOY ARGUMENT THAT ITS PRACTICES CORRESPOND TO LOCAL DEMAND, EMBASSY MAY WISH TO POINT OUT THAT CONSUMER DEMAND (IN THE SENSE OF QUANTITY OF PRODUCT DEMANDED) IS A FUNCTION OF PRICE.

5. ACTION REQUESTED: EMBASSY IS REQUESTED TO SUBMIT ABOVE CASE TO TFC, UNLESS IT IS AWARE OF INFORMATION CONTRARY TO THE FACTS AS PRESENTED. VANCE

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Message Attributes

Automatic Decaptioning: X
Capture Date: 26 sep 1999
Channel Indicators: n/a
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Concepts: TRADE, TOBACCO, COMMITTEES
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Decaption Date: 01 jan 1960
Decaption Note:
Disposition Action: n/a
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment:
Disposition Date: 01 jan 1960
Disposition Event:
Disposition History: n/a
Disposition Reason:
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Enclosure: n/a
Executive Order: N/A
Errors: n/a
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Review Release Date: N/A
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
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To: TOKYO INFO GENEVA
Type: TE
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